

**Secret**



DIRECTORATE OF  
INTELLIGENCE

# Intelligence Report

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43

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## WARNING

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C O N T E N T S

	<u>Page</u>
1. Sweden . . . . .	1
2. Insurgency in Kalimantan (Indonesian Borneo) . . . . .	2
3. Indonesia . . . . .	3
4. Japan - South Korea . . . . .	4

6 November 1967

SECRET

1. SWEDEN

Swedish-US relations are likely to continue to deteriorate because of the exploitation of the Vietnam war for domestic political gain by Prime Minister Erlander's minority Social Democratic government.

Developments at the Social Democrats' recent special congress, and especially the resolution it passed on Vietnam harshly critical of the US, made it clear that the moderate leadership has acceded to left-wing pressure to "radicalize" the party program, especially in the foreign policy field, in preparation for next year's national elections. The objective of the congress was to bolster the party's waning political fortunes. By adopting a more "activist" image on such issues as the Vietnam war, which is viewed with widespread aversion in Sweden, the leadership hopes to counter mass defections to the revitalized Swedish Communist party.

The rising influence of the Communists under Carl-Henrik Hermansson and the minority position of the Erlander government have led to speculation about closer cooperation between the two parties should next September's elections result in further losses for the Social Democrats and gains for the Communists. In that case the Social Democrats would have to decide whether to invite the Communists to participate in the government. The likelihood of this development would be increased if the 66-year-old Erlander retired after the election and was succeeded by his protégé, the controversial young minister of education, Olof Palme, who has assumed the role of spokesman for those hostile to US policy in Vietnam.

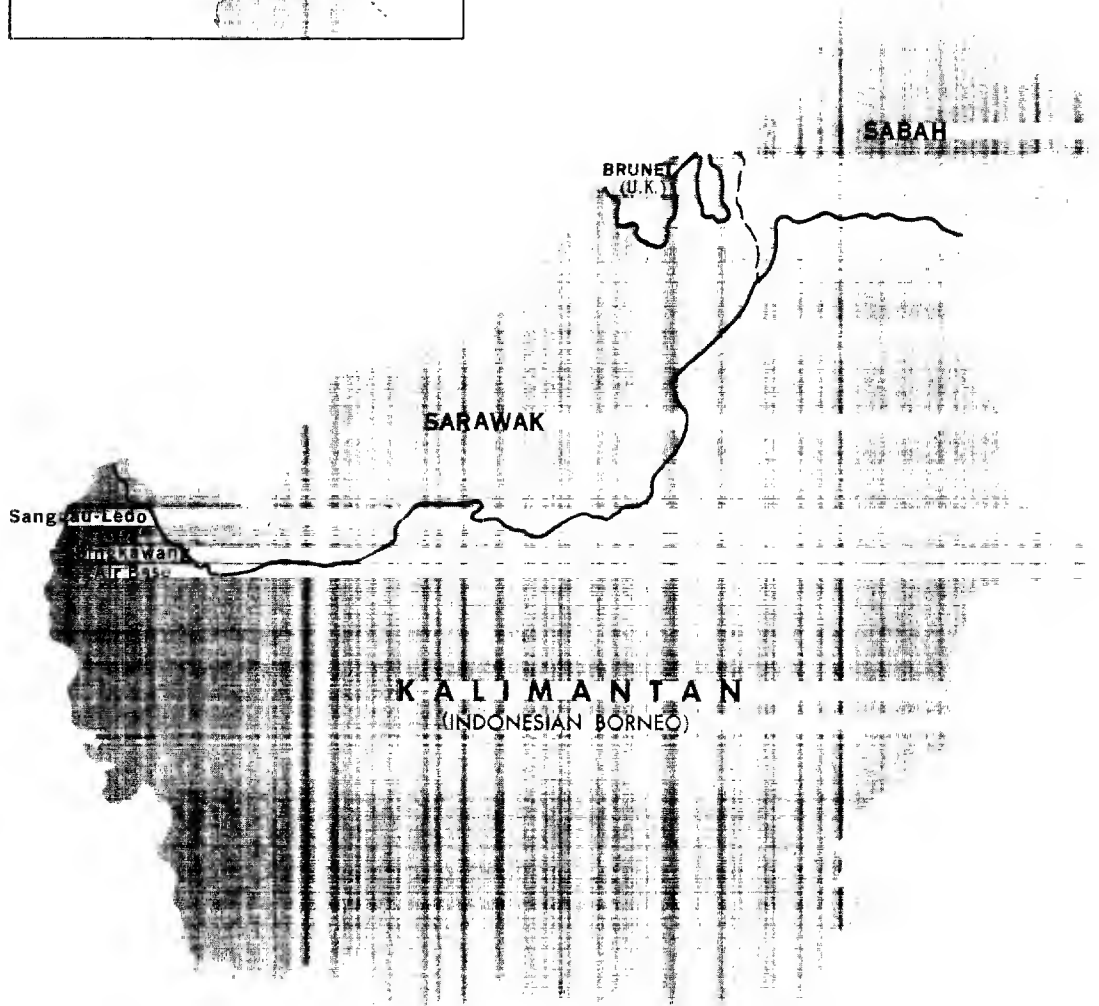
This generally negative trend in Swedish-US relations comes at a time when the direction of Stockholm's foreign policy has increasingly slipped from the control of professionals in the Foreign Ministry to radical elements who are prepared to use it to advance partisan political objectives. [REDACTED]

[REDACTED]

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# BORNEO



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2. INSURGENCY IN KALIMANTAN (INDONESIAN BORNEO)

A Communist guerrilla movement in Indonesian Borneo is causing problems for security forces there, and poses a potential threat to East Malaysia (see map).

The guerrillas, members of the Sarawak Communist Organization (SCO) and numbering about 800, are anti-Malaysian Chinese [REDACTED]

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Since the formal end of confrontation last year they have resisted Indonesian attempts to neutralize them and have remained on the Indonesian side of the border with Malaysia. They are now engaging Indonesian troops in an effort to develop a liberated area from which to launch an eventual guerrilla campaign in support of anti-Malaysia elements in Sarawak.

The guerrillas have accelerated their military activity since July 1967, when they raided Singkawang Air Base and captured 100 assorted weapons. Recent ambushes, primarily in the Sanggau-Ledo area, have cost Djakarta approximately 50 dead.

Indonesian reinforcements have brought troop strength in the area to approximately five battalions. Military operations, however, are hampered by inadequate logistics and communications. [REDACTED]

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Although guerrilla elements now constitute only a localized security problem, this could increase and spread should the guerrillas gain the support and further sympathy of the sizable Chinese minority in the area. While there is no evidence that the Chinese are giving the guerrillas material support, the SCO in Sarawak has established contact with Peking. [REDACTED]

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3. INDONESIA

Although some progress has been made since Indonesia announced major economic reform measures nearly a year ago, the effect of many years' mismanagement is still felt and no significant economic growth has been registered.

The hyperinflation that previously pervaded the economy has been halted, primarily by cutting back government expenditures and improving the collection of revenue. This policy has had little if any effect, however, in raising domestic production.

Foreign economic relations have improved considerably. Foreign enterprises taken over by the former regime now have been returned to their owners. Direct foreign investment, previously forbidden, is welcomed as are joint ventures between Indonesian and foreign firms.

Western creditors who agreed to reschedule Indonesia's outstanding debts also agreed to provide about \$200 million in the form of import credits during 1967. This month these Western creditors will consider further aid commitments for 1968. Indonesia hopes to receive \$325 million. Failure to obtain this level of assistance would delay urgently needed rehabilitation of facilities, such as the transportation system, necessary for any future economic growth and to attract private investment.

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#### 4. JAPAN - SOUTH KOREA

Japan is rapidly increasing its financial stake in South Korea's development. It probably will dislodge the US as the primary source of foreign economic assistance in the early 1970s.

A recent agreement by Japan to extend \$200 million in commercial credits raises the total amount of assistance promised South Korea since the 1965 Normalization Treaty to \$1 billion. This assistance combined with the prospect for direct Japanese investment will significantly enlarge Japan's role in Korean economic development.

Under the 1965 Normalization Treaty Japan agreed to provide South Korea \$500 million in grants and soft term loans to satisfy Korean reparation claims against Japan and \$300 million in commercial credits. These commercial credits include \$90 million for the Korean fishing industry, \$30 million for the purchase of Japanese merchant ships, and \$180 million for industrial machinery and equipment. An additional \$200 million in commercial credits was promised to Korea in August at the ministerial conference in Tokyo. Japan also agreed at that time to help reduce Korea's large trade imbalance by increasing imports from about \$66 million in 1966 to a planned level of \$300 million by 1971.

South Korea also recently approved the first Japanese equity investment in a machine tool plant in Pusan. Seoul's recently liberalized incentives for foreign private investment and the opening of Japan's first branch bank in South Korea will provide further stimulus to Japanese private investment.

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